Customs in GST context – Taxing global trade transactions

Supply chain at the border – One transaction, two taxes

There is a strong interplay of GST and customs laws in relation to international trade transactions – both export and import, because of various changes such as:

- Components and rates of customs duty computation;
- Change in method of computation;
- Change in policy around customs duty exemptions;
- Change in credit eligibility of IGST paid at the time of import

Customs duty has two components, i.e., basic customs duty ('BCD') and IGST; BCD is not creditable and hence becomes a cost, while IGST is creditable and therefore could be cash flow issue for business. Effective median rate of customs duty has split into a few slabs (depending on the IGST rates of 5%, 12%, 18% and 28%). Accordingly, as against the pre-GST customs duty median rate of approximately 26%, the post GST median rate could range up to approximately 37%.

Method of IGST computation for customs duty purposes has changed from that adopted for CVD and SAD in the past. IGST is computed on the assessable value, as against the differential mechanism prescribed hitherto for products covered under legal metrology and MRP regulations. This will also have a direct impact on the effective customs duty payable on imported goods.

In the past, Government policies/ initiatives were implemented through CVD and SAD exemptions. However, exemptions are no more the norm as it is against the basic construct of GST and is seen as disrupting the credit chain. It is expected that IGST exemptions on import of goods would be minimal as compared to the past.

IGST credit eligibility policy is more generous and less restrictive. It impacts different businesses in different ways – credit of CVD and SAD was not available for an import and sale business but IGST credits

How Deloitte can help

Our team of Customs and Global Trade specialists, along with a strong GST team, has the expertise to handhold/guide your organization and help identify and resolve conflicts between customs and GST. Deloitte support would include:

- Advising on interplay of business facts with customs laws and procedures and that of GST;
- Assisting in business restructure, to align the customs and GST functions;
- Devising appropriate internal controls/ processes to manage the risks arising from introduction of GST on the global trade function;
- Identifying areas of efficiency;
- Revisiting the export incentives, duty exemptions and working capital efficiency

With our worldwide presence and a coordinated Customs and Global Trade team, we endeavor to bring significant value and insight on the table from our global GST experience, which can be of assistance to devise medium/long term strategies for the global trade.

would be eligible on a go forward basis. Similarly, the SAD element which was not available as a credit for service providers, would no more be a cost in the supply chain.

Aspects of GST interplay with customs

The strong interplay of GST and customs has the following dimensions:

1. **Taxable event –** International trade creates a mirage of two taxable events on the same transaction – that of 'supply' under GST law and 'import' or 'export', as the case may be, under Customs law. The primary question to be answered is – "When does an event of bringing the goods from outside India into India become a taxable event under GST law?" A clear perspective and position on the taxable event vis-à-vis specific business transaction is very much at the core of being able to correctly identify consequent compliances and obligations.
2. **Common language of classification –** GST adopts the global language of classification of goods, based on the Harmonised System of Nomenclature (HSN) at a four digit level while Customs adopts the same classification at an eight digit level. Adopting the customs classification (including HSN code) for GST purposes, and variances (if any) is an important consideration for consistency in compliances.
3. **Valuation –** Transaction value of imported goods will continue to influence 'in-bond sale transactions' before clearance from customs frontier and so would be the case for export goods where incentives and refund claims will have a bearing on customs valuation of goods in the shipping bill. .
4. **Input credit of import duty –** IGST paid at the time of import is available as credit down the domestic supply chain and hence import documents remain an important part of GST credit chain for imported goods. Similarly, GST embedded in export goods is to be reclaimed by the exporter on the basis of export documents filed with customs.
5. **Export incentives and related exemptions –** The domestic supply chain is directly impacted by GST while international supply chain is impacted by various export incentives and export related import exemptions. GST credit chain disruption would strongly influence decision around incentives and exemptions.

Hitherto, the integration of the customs and tax function was limited to availment of credit of custom duties. Going forward, the customs function of companies/importers will need closer coordination with the tax function.

Managing the changing dynamics of global trade transactions

Businesses will have to revisit the rule of thumb and decision matrix for global trade transactions, especially at the point of intersection of domestic and international trade supply chain. The customs function within an organization, which is (generally) managed by the operations team, will now require active and continuous support of the tax teams also. Unlike VAT, excise and service tax legislations, GST laws is a continuation of the global trade transaction, where the goods merge or exit from the domestic transaction.

The key features of GST structure such as reduced number of exemptions to ensure integrity of credit chain and increased credit flow through the supply chain, will also have a bearing on pricing, cost and working capital requirement for managing the cross border supply chain.

Tax administration will also look at the tax law with a fresh perspective and fresh cause of disputes may emerge which will need to be handled based on first principles and without extensive support from past jurisprudence. To be able to manage this change, businesses will require increased focus and a strong interdisciplinary approach for identifying and articulating the news ways of working through trade transactions.